

## Message Text

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ACTION NEA-10

INFO OCT-01 ISO-00 CIAE-00 DODE-00 PM-04 H-01 INR-07 L-03  
NSAE-00 NSC-05 PA-01 PRS-01 SP-02 SS-15 USIA-06  
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-----260907Z 048538 /15

R 260820Z JAN 77  
FM AMEMBASSY TEL AVIV  
TO SECSTATE WASHDC 4574

C O N F I D E N T I A L TEL AVIV 0571

E.O. 11652: GDS  
TAGS: EFIN, IS  
SUBJECT: RABINOWITZ ON THE 1977 BUDGET

REF: TEL AVIV 560

1. SUMMARY: FINANCE MINISTER RABINOWITZ DOES NOT ANTICIPATE REAL DIFFICULTY IN THE KNESSET IN GETTING BUDGET AUTHORIZATION FOR AN INTERIM PERIOD AFTER THE NEW FISCAL YEAR BEGINS ON APRIL 1. HE SAID THAT ALTHOUGH THE GOVERNMENT OF COURSE DID NOT HAVE A MAJORITY, EITHER IN THE FINANCE COMMITTEE OR IN THE FULL KNESSET, HE EXPECTED TO GET APPROVAL FOR EXPENDITURES OVER A THREE TO SIX MONTH PERIOD AT AN ACCEPTABLE LEVEL. THE BUDGET CONTINUES THE POLICY OF RESTRAINT, HE SAID, AND IS DESIGNED TO IMPROVE THE BALANCE OF PAYMENTS, CURB INFLATION AND CREATE CONDITIONS FOR RENEWED GROWTH NEXT YEAR. END SUMMARY.

2. IN A MEETING ON JANUARY 25, RABINOWITZ TOLD US THAT THE GOVERNMENT COULD POINT WITH PRIDE TO SEVERAL ACCOMPLISHMENTS OVER THE PAST YEAR: EXPORTS WENT UP 28 PER CENT, INDUSTRIAL OUTPUT HAD RISEN FIVE TO SIX PER CENT, INDUSTRIAL INVESTMENT HAD GONE UP 18 PER CENT IN 1975 AND HAD DROPPED BY ONLY FOUR PER CENT IN 1976, TOURISM HAD  
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INCREASED SIGNIFICANTLY, AND THERE HAD BEEN AN \$800 MILLION REDUCTION IN THE BOP CURRENT ACCOUNT DEFICIT. THE DROP IN HOUSING CONSTRUCTION AND IN LOCAL MILITARY EXPENDITURE, HOWEVER, HAD BEEN SUFFICIENT TO OFFSET MUCH OF THE EXPANSION IN OTHER SECTORS WITH THE RESULT THAT THE GNP IN 1976 PROBABLY ROSE BY ONLY ONE TO TWO PER CENT. HE NOTED, IN THIS REGARD, THAT IF THE MILITARY SECTOR

WERE EXCLUDED, GNP WOULD SHOW AN INCREASE OF THREE PER CENT IN 1976 (SUFFICIENT DATA FOR A DEFINITIVE CALCULATION OF GNP WOULD NOT BE AVAILABLE FOR SEVERAL MONTHS).

3. WHEN QUERIED ABOUT THE INFLATIONARY IMPACT OF THE BUDGET AND, IN PARTICULAR, WHETHER THE BUDGET ASSUMED THAT A PACKAGE AGREEMENT ON WAGES AND PRICES WOULD BE AGREED, RABINOWITZ REPLIED THAT THE BUDGET STOOD ON ITS OWN AND IN HIS OPINION WAS NOT INFLATIONARY. HE WAS STILL TRYING TO WORK OUT AN AGREEMENT ON A WAGE/PRICE PACKAGE BUT WAS PESSIMISTIC THAT IT COULD BE ACHIEVED BEFORE THE ELECTIONS. HE NOTED, HOWEVER, THAT HISTADRUT HAD AGREED TO ESTABLISH AN ARBITRATION BOARD FOR DEALING WITH LABOR DISPUTES IN THE PUBLIC SECTOR. THIS WAS A SIGNIFICANT STEP IN THE RIGHT DIRECTION SINCE LABOR UNREST WAS CENTERED IN THE PUBLIC SECTOR. REAL WAGES THERE HAD DROPPED 15 PER CENT OVER THE LAST THREE YEARS, WHEREAS PRIVATE SECTOR WORKERS HAD OBTAINED SIGNIFICANT INCREASES IN REAL WAGES.

4. ON THE QUESTION OF PRICE INCREASES, RABINOWITZ SAID THAT THE GOVERNMENT HAS A FIRM TARGET OF REDUCING THE INFLATION RATE FROM LAST YEAR'S 38 PER CENT TO 25 PER CENT THIS YEAR AND TO 15 PER CENT IN 1978 (FIGURES REPRESENT PRICE RISES DURING THE YEAR RATHER THAN AVERAGE RATES.) LAST YEAR'S INFLATION, HE MAINTAINED, WAS PRIMARILY COST-PUSH RATHER THAN DEMAND-PULL, REFLECTING DEVALUATION, VAT AND THE CUT INSUBSIDIES FOR THE MOST PART. THIS YEAR THERE WOULD BE LESS DEVALUATION AND NO

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INCREASE IN VAT.

5. THE PROPOSED DEFENSE BUDGET WAS ABOUT THREE PER CENT LOWER THAN LAST YEAR'S BUDGET IN REAL TERMS, AND REPRESENTED ONLY 33 PER CENT OF THE TOTAL BUDGET COMPARED TO 39 PER CENT IN 1976. PER CAPITA PRIVATE CONSUMPTION WOULD NOT INCREASE AT ALL IN 1976, HE SAID, AND THERE WOULD BE SOME SOFTENING OF THE LABOR MARKET.

6. COMMENT: THIS BUDGET NOT ONLY IS LESS RESTRICTIVE THAN ISRAEL'S ECONOMIC SITUATION WOULD SEEM TO WARRANT BUT ALSO FALLS SHORT OF WHAT A NUMBER OF SENIOR FINANCE MINISTRY OFFICIALS THEMSELVES WANTED (AS REFLECTED IN OUR PREVIOUS REPORTING). DESPITE THE LARGE BUDGET DEFICIT (WHICH MAY IN FACT BE REDUCED SOMEWHAT TO GAIN SUPPORT IN THE KNESSET) AND THE ABSENCE OF INCENTIVE FOR EEEDED STRUCTURAL CHANGE, THE PROPOSAL WOULD NOT BE TOO BAD IF THERE WERE ANY ASSURANCE THAT IT WOULD IN FACT BE ADHERED TO OVER THE BUDGET YEAR AND THAT A MEANINGFUL WAGE/PRICE

AGREEMENT COULD BE REACHED WITH HISTADRUT AND THE EMPLOYERS. UNFORTUNATELY, NEITHER OF THE LATTER IS LIKELY TO BE REALIZED AND THERE IS LITTLE EXPECTATION THAT THE ELECTIONS WILL CHANGE THINGS VERY MUCH.  
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## Message Attributes

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